

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF ILLINOIS

IN RE:

CLIFFORD SAMUEL KIRBY, JR. and
SHERRY LORAIN KIRBY,

Bankruptcy Case No. 01-60020

Debtors.

CLIFFORD SAMUEL KIRBY, JR.,

Plaintiff,

vs.

Adversary Case No. 02-6025

FIRST NATIONAL BANK OF
DIETERICH,

Defendant.

OPINION

This matter having come before the Court for trial on a Complaint for Sanctions Against First National Bank of Dieterich filed by Plaintiff, Clifford Samuel Kirby, Jr.; the Court, having heard sworn testimony and arguments of counsel and being otherwise fully advised in the premises, makes the following findings of fact and conclusions of law pursuant to Rule 7052 of the Federal Rules of Bankruptcy Procedure.

Findings of Fact

The material facts in this matter are largely undisputed and are, in pertinent part, as follows:

The Debtor/Plaintiff previously operated a business known as "Kirbyco, Inc." which filed for relief

under Chapter 7 of the Bankruptcy Code on December 29, 2000, in Case No. 00-61088. The First National Bank of Dieterich (FNBD) was scheduled as a creditor in the Kirbyco, Inc. bankruptcy holding a secured claim in the amount of \$226,159.06. Debtor/Plaintiff was also scheduled in the Kirbyco, Inc. bankruptcy as a co-debtor on the debts owed to FNBD. The uncontroverted evidence adduced at trial indicated that the Debtor/Plaintiff not only signed the note underlying the FNBD debt as an officer of Kirbyco, Inc., but also signed as a personal guarantor of that note. Although Kirbyco, Inc. did not receive a discharge, as it was a corporate entity, the Chapter 7 case of Kirbyco, Inc. was duly administered and subsequently closed.

In addition to the financial difficulties experienced by Kirbyco, Inc., the Debtor/Plaintiff experienced personal financial problems. As a result, he filed the instant Chapter 7 proceeding on behalf of himself and his wife, on January 24, 2001. The Debtor/Plaintiff scheduled FNBD as a secured creditor holding a claim in the amount of \$211,852.72, in his personal Chapter 7 bankruptcy, based upon his personal guarantee of the debt of Kirbyco, Inc. discussed above. FNBD received due and appropriate notice of the Debtor/Plaintiff's personal Chapter 7 bankruptcy, and a discharge was entered pursuant to 11 U.S.C. § 524 on May 1, 2001, covering all of the dischargeable debt scheduled in Debtor/Plaintiff's personal Chapter 7 bankruptcy proceeding, including the debt to FNBD. There is no dispute that FNBD received due and appropriate notice of the entry of the discharge in the Debtor/Plaintiff's personal Chapter 7 bankruptcy case.

In April 2001, in furtherance of his desire to restart his business, Debtor/Plaintiff approached FNBD with an offer to purchase equipment previously owned by Kirbyco, Inc., which FNBD held as collateral on its secured debt that had been scheduled in both the Kirbyco, Inc. Chapter 7 proceeding and in the Debtor/Plaintiff's personal bankruptcy case. On April 27, 2001, after negotiations between the

Debtor/Plaintiff and FNBD, it was agreed that the Debtor/Plaintiff would be allowed to purchase the equipment for the sum of \$25,000. To finance the purchase of the equipment, FNBD agreed to loan Debtor \$25,000, which was evidenced by a note designated as "Loan No. 106493." The entire amount of the proceeds of Loan No. 106493 was paid directly by FNBD against the balance due on the \$211,852.72 secured debt which had been scheduled in both the Kirbyco, Inc. bankruptcy and in the Debtor/Plaintiff's personal bankruptcy. The Debtor/Plaintiff was not represented by legal counsel during the negotiation and/or execution of the equipment loan.

Following the purchase of the Kirbyco, Inc. equipment, the Debtor/Plaintiff began to once again operate his business. In late June or early July 2001, Debtor/Plaintiff contracted for a job in Wheeling, Illinois. In order to perform the Wheeling job, the Debtor/Plaintiff needed cash to make payroll and finance other expenses of the job. Sometime on or before July 11, 2001, Debtor/Plaintiff contacted FNBD to request an \$8,000 loan to finance the Wheeling job. FNBD, believing that Debtor/Plaintiff could not get credit elsewhere, agreed to loan Debtor/Plaintiff the \$10,000 in new cash in exchange for Debtor/Plaintiff's execution of a new note in the amount of \$231,590.66, together with an assignment on accounts receivable of Debtor/Plaintiff from a company known as "Amtec Engineering of Houston, Texas." The new note was designated as "Loan No. 106748." From the proceeds of the new loan, Debtor/Plaintiff received \$10,000 cash, with the remaining amount of the loan being paid directly by FNBD against the balance of the secured debt scheduled in the Kirbyco, Inc. bankruptcy proceeding and in Debtor/Plaintiff's personal bankruptcy proceeding. FNBD does not dispute that the purpose for entering into Loan No. 106748, on August 21, 2001, was to do away with the old large indebtedness of Debtor/Plaintiff. Both the Debtor/Plaintiff and FNBD were hopeful that an account receivable of Kirbyco, Inc. that was in litigation would eventually provide proceeds that would greatly reduce the new indebtedness.

The evidence adduced at trial indicates that Debtor/Plaintiff made voluntary payments on the equipment loan in the amount of \$5,732.48, but eventually he fell behind in payments due FNBD on the equipment loan. In 2002, Debtor/Plaintiff's business faltered, and, on June 29, 2002, an auction was held in which the equipment securing the equipment loan was sold. A portion of the proceeds of the auction, in the amount of \$21,790.56, was applied by FNBD to pay off the equipment loan.

In addition to the monies which were received by FNBD, both through voluntary payment of Debtor/Plaintiff and through the equipment auction on June 29, 2002, FNBD debited Debtor/Plaintiff's account in the amount of \$21,000 on September 18, 2001. This debit by FNBD was done without the consent of Debtor/Plaintiff and over his objection. The purpose of the debit was to pay back the new \$10,000 in cash which Debtor/Plaintiff had received in April 2001, with the remaining \$11,000 being applied to Loan No. 106748. FNBD also received the sum of \$119,350 from the settlement of an account receivable in which it held a security interest under the Kirbyco, Inc. debt. There is no dispute that FNBD was entitled to the entire amount from the settled account receivable, and that said amount was rightfully applied to the debt owed FNBD. After application of all monies received by FNBD, a balance continued to exist on Loan No. 106748, and FNBD continued to pursue collection of that balance, resulting in the filing of the instant adversary proceeding by the Debtor/Plaintiff on October 8, 2002.

Conclusions of Law

In this proceeding, Debtor/Plaintiff seeks a determination that FNBD is in civil contempt for having violated and disregarded the terms of 11 U.S.C. §524 and the discharge order entered in his personal Chapter 7 bankruptcy case. The Debtor/Plaintiff also seeks an order from the Court enjoining FNBD from any further action or attempt to collect amounts it claims due on debt remaining on Loan No. 106748. Additionally, the Debtor/Plaintiff seeks a judgment against FNBD for willful and wanton violation of the

discharge injunction under 11 U.S.C. §524, with actual damages in the amount of \$26,732.48, attorney's fees and costs in the amount of \$5,738.01, and \$80,197.44 in punitive damages.

A review of the undisputed facts in this matter leads the Court to conclude that FNBD did violate the permanent discharge injunction under 11 U.S.C. §524, by requiring the Debtor/Plaintiff to enter into Loan No. 106748, on August 21, 2001. While there was no violation in entering into the equipment loan, No. 106493, and entering into a loan arrangement for the \$10,000 in new cash which the Debtor/Plaintiff received on August 21, 2001, there was a violation in requiring the Debtor/Plaintiff to sign Loan No. 106748 for amounts in excess of the \$10,000 in new cash that he received.

The provisions of 11 U.S.C. §524 are clear. The old debt due FNBD in excess of \$200,000 left over after the Kirbyco, Inc. bankruptcy and Debtor/Plaintiff's personal bankruptcy was clearly personal debt of the Debtor/Plaintiff which was discharged by order of this Court on May 1, 2001. The Bankruptcy Code provides a means by which a creditor and a debtor can agree to the repayment of pre-petition debt that would otherwise be discharged in a Chapter 7 proceeding. Title 11 U.S.C. §524(c) sets forth specific requirements which must be met before a pre-petition debt can be reaffirmed, thereby obligating the debtor to repay it in spite of his discharge. See: In re Vazquez, 221 B.R. 222 (Bankr. N.D. Ill. 1998); In re Smith, 224 B.R. 388 (Bankr. N.D. Ill. 1998); and In re Mickens, 229 B.R. 114 (Bankr. W.D. Va. 1999). In the instant case, there was no reaffirmation agreement entered into between FNBD and Debtor/Plaintiff.

It is undisputed that one of the purposes of Loan No. 106748 was to retire old debt to FNBD that had been scheduled in the Kirbyco, Inc. bankruptcy and discharged in the Debtor/Plaintiff's personal bankruptcy. The facts clearly show that \$221,515.66 of the proceeds of Loan No. 106748 were paid directly by FNBD against the balance of the old debt. In fact, FNBD stated purpose in entering into Loan

No. 106748 was to "do away with the old large indebtedness" of Kirby. See: Request to Admit Paragraph 39 and Kirby Exhibit M.

While 11 U.S.C. §524(f) allows a debtor to voluntarily repay his pre-petition debts, the facts of this case indicate that some of the post-petition payments made to FNBD were not voluntary. As stated above, the Court finds that FNBD was not in violation of the permanent discharge injunction by entering into the \$25,000 equipment loan, nor by entering into a loan with the Debtor/Plaintiff for \$10,000 in new cash. However, FNBD was in violation of the permanent discharge injunction when it required the Debtor/Plaintiff to enter into Loan No. 106748 for amounts in excess of the \$10,000 in new cash, and any payments received for amounts claimed due above and beyond the \$25,000 equipment loan and the \$10,000 in new cash were not voluntary. Specifically, the Court finds that the \$21,000 debit against Debtor/Plaintiff's account at FNBD, on September 18, 2001, was not voluntary, and \$11,000 from this debit was clearly applied against pre-petition debt which had been discharged.

In analyzing Debtor/Plaintiff's request for damages, the Court finds that FNBD has engaged in a willful violation of the permanent discharge injunction as a result of its attempts to collect on indebtedness discharged in Debtor/Plaintiff's personal Chapter 7 bankruptcy proceeding. However, much of the money received by FNBD was properly paid toward and applied to new debt. The \$5,732.48 paid by the Debtor/Plaintiff on the equipment loan, as evidenced by Debtor/Plaintiff's Exhibit O, was properly credited against new debt. Similarly, the \$21,790.56 of proceeds from the equipment auction of June 29, 2002, applied by FNBD to pay off the equipment loan was for new debt and not in violation of the permanent discharge injunction. The Court also concludes that \$10,000 of the \$21,000 debit of September 18, 2001, against Debtor/Plaintiff's account at FNBD was properly charged against the \$10,000 in new cash which the Debtor/Plaintiff had received on August 21, 2001. The remaining \$11,000 of the \$21,000 debit which

was applied against the balance of Loan No. 106748 was, however, an improper transaction and clearly in violation of the permanent discharge injunction under 11 U.S.C. §524.

In addition to seeking actual damages, Debtor/Plaintiff seeks punitive damages in the amount of \$80,197.44. Numerous factors must be considered in determining whether punitive damages are appropriate for a creditor's violation of the discharge injunction. As stated in Vazquez, supra, at 231, Courts must consider (1) the nature of the creditor's conduct; (2) the creditor's ability to pay damages; (3) the motive of the creditor; and (4) any provocation by the debtor. Punitive damages are generally awarded in response to particularly egregious conduct on behalf of a creditor. See: Vazquez, supra, at 231, *citing In re Gault*, 136 B.R. 736 (Bankr. E.D. Tenn. 1991), and *In re Wagner*, 74 B.R. 898 (Bankr. E.D. Pa. 1987). Most Courts that have awarded punitive damages for a violation of the discharge injunction require actions taken with either a malevolent intent or a clear disregard and disrespect of the bankruptcy laws. It is not sufficient to merely show that a creditor's actions were deliberate. In re Arnold, 206 B.R. 560 (Bankr. N.D. Ala. 1997). In the instant case, the Court finds that, while the conduct of FNBD was clearly deliberate, there is no evidence of a malevolent intent or a clear disregard and disrespect of the bankruptcy laws. In fact, it appears that, while FNBD improperly required the Debtor/Plaintiff to sign a note obligating him for pre-petition discharged indebtedness, both parties were hopeful that an account receivable in litigation would yield sufficient funds to either greatly reduce or entirely retire the indebtedness. Thus, the Court must conclude that, while the Debtor/Plaintiff is entitled to be reimbursed for his actual damages, attorney's fees, and costs, punitive damages under the facts of the instant case are not appropriate.

In determining appropriate damages in this case, the Court finds that the sum of \$11,000 debited from Debtor/Plaintiff's account at FNBD, on September 18, 2001, was improperly applied against old indebtedness which had been discharged in Debtor/Plaintiff's personal Chapter 7 bankruptcy proceeding.

As such, the Court finds that the Debtor/Plaintiff is entitled to a judgment in the amount of \$11,000. The Court also finds that the Debtor/Plaintiff has properly shown that he is entitled to an award for attorney's fees and costs in the amount of \$5,738.01.

ENTERED: May 28, 2003.

/s/ Gerald D. Fines
United States Bankruptcy Judge